Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matter of	)	
	)	
Rulemaking to Amend Parts 1. 2, 21, and 25	)	CC Docket No. 92-297
of the Commission's Rules to Redesignate	)	
the 27.5-29.5 GHz Frequency Band, to	)	
Reallocate the 29.5-30.0 GHz Frequency	)	
Band, to Establish Rules and Policies for	)	
Local Multipoint Distribution Service and	)	
for Fixed Satellite Services	)	

Comments
of the
Competition Policy Institute

Ronald Binz
Debra Berlyn
John Windhausen

Competition Policy Institute
1156 15th St. N.W. Suite 310
Washington, D.C. 20005
Phone: 202 835-0202
Fax: 202 835-1132

August 12, 1996

Summary

CPI is a non-profit organization that advocates state and federal regulatory policies to bring competition to energy and communications markets in ways that benefit consumers. CPI believes that competition will lead to reduced regulations, new technologies, higher service quality, and lower prices for consumers.

Local Multipoint Distribution Service (LMDS) has the potential to provide significant facilities-based competition to both incumbent local exchange carriers (ILECs) and incumbent cable operators (ICOs). LMDS could give consumers a new choice for video and telephony services and could bring into reality the vision endorsed by Congress and the President of a competitive marketplace for all telecommunications and information services. At the same time, the market and technology for LMDS are in their infancies. The Commission should not lose the opportunity at this stage, before entrenched service providers become heavily invested in the technology or the licenses, to adopt the most pro-competitive, pro-consumer policies for this new service.

CPI thus believes that the Commission should prevent both the ILEC and the ICO from obtaining an LMDS license in the area where they currently provide service. First, an eligibility restriction would encourage the introduction of a third new competitor in each market for video and telephony services, a result that is consistent with the goal of the Telecommunications Act of 1996. Second, a new entrant will have the maximum incentives to develop the full potential of the technology. If the ILEC or ICO is allowed to own the LMDS license where it already provides service, it may choose to use LMDS only to supplement one of its existing service offerings, or, worse, may retard the provision of certain services to consumers in order to protect its existing network investments. CPI believes that this eligibility restriction should expire once the ILEC or the ICO faces enough competition that it has the same incentives to maximize the development of the LMDS technology and services as any other company.

COMMENTS OF THE
COMPETITION POLICY INSTITUTE
CONCERNING ELIGIBILITY RESTRICTIONS
FOR LMDS LICENSES

The Competition Policy Institute (CPI) submits these comments in response to the Commission's Fourth Notice of Proposed Rulemaking in CC Docket No. 92-297 concerning eligibility restrictions for licenses for Local Multipoint Distribution Service (LMDS) providers.

CPI is a non-profit organization that advocates state and federal regulatory policies to bring competition to energy and communications markets in ways that benefit consumers. CPI believes that competition will lead to reduced regulations, new technologies, higher service quality, and lower prices for consumers.

I. Introduction and Summary

Local Multipoint Distribution Service (LMDS) has the potential to provide significant facilities-based competition to both incumbent local exchange carriers (ILECs) and incumbent cable operators (ICOs). LMDS could give consumers a new choice for video and telephony services and could bring into reality the vision endorsed by Congress and the President of a competitive marketplace for all telecommunications and information services. At the same time, the market and technology for LMDS are in their infancies. The Commission should not lose the opportunity at this stage, before entrenched service providers become heavily invested in the technology or the licenses, to adopt the most pro-competitive, pro-consumer policies for this new service.

CPI thus believes that the Commission should prevent both the ILEC and the ICO from obtaining an LMDS license in the area where they currently provide service. First, an eligibility restriction would encourage the introduction of a third new competitor in each market for video and telephony services, a result that is consistent with the goal of the Telecommunications Act of 1996. Second, a new entrant will have the maximum incentives to develop the full potential of the technology. If the ILEC or ICO is allowed to own the LMDS license where it already provides service, it may choose to use LMDS only to supplement one of its existing service offerings, or, worse, may retard the provision of certain services to consumers in order to protect its existing network investments. CPI believes that this eligibility restriction should expire once the ILEC or the ICO faces enough competition that it has the same incentives to maximize the development of the LMDS technology and services as any other company.

These positions are discussed in more detail below.

II. Eligibility restrictions will promote competition, a goal endorsed by Congress in enacting the Telecommunications Act of 1996.

In enacting the Telecommunications Act of 1996, Congress and the President expressed a clear preference for policies that promote competition. This is particularly true for telephony and video services, which are usually provided today by companies that have a monopoly, or at least market power, in their local markets. The Telecommunications Act is replete with provisions that encourage a more competitive marketplace for video and telephony, including provisions that

- impose requirements on ILECs to open and unbundle their networks for competitors (Section 251);
- preempt State and local laws that prohibit or have the effect of prohibiting competition for telecommunications services (Section 253);

- promote nondiscriminatory accessibility to public telecommunications networks by the broadest number of users and vendors of products and services (Section 256);
- permit affiliates of public utility holding companies to provide telecommunications; (Section 103);
- prohibit the Regional Bell Operating Companies (RBOCs) from providing interLATA service until they face competition from a facilities-based provider to business and residential customers (Section 271); and,
- generally prohibit ILECs and ICOs from acquiring one another or from entering into joint venture agreements in the same markets.

It is also clear that Congress did not intend to place a limit on the FCC's authority to take further action to enhance competition. Congress did not include any provisions specifically restricting the FCC's ability to take other pro-competitive decisions, as it did in some other provisions.[1] In fact, by retaining and enhancing the "public interest" standard in the Communications Act, Congress confirmed that the FCC has a substantial amount of discretion to develop policies consistent with the goal of promoting competition. Further, Section 257 specifically directs the Commission through a rulemaking proceeding to eliminate market entry barriers for entrepreneurs and other small businesses in the provision and ownership of telecommunications services and information services.[2]

---

[1] For instance, Congress directed that the FCC could not expand the list of items contained in the "competitive checklist" that an RBOC must satisfy before being granted entry into the interLATA market. See Section 271(d)(4).

[2] In addition to promoting opportunities for small businesses and entrepreneurs, subsection 257(b) states that, "[i]n carrying out subsection (a), the Commission shall seek to

CPI believes that preventing the ILECs and ICOs from acquiring the LMDS license in a market will serve the Congressionally-endorsed goal of promoting competition. As the Commission itself noted, "We expect that LMDS providers will offer facilities-based competition to traditional cable and telephone carriers -- greatly enhancing customer choice, and facilitating the rapid dissemination of innovative communications services with the entry of multiple providers into the market."[3] The ILECs and ICOs often have monopoly, or market, power over telecommunications services and video services in the local market. If one or both of these incumbents are permitted to acquire the LMDS license in their service territories, the market will be less competitive than if a new entrant acquires that license.

The logic for promoting the entry of a third competitor in a market is almost identical to the logic that led Congress to prevent ILECs or ICOs operating in the same market from acquiring each other or engaging in joint ventures.[4] In that case, Congress sought to promote competition between the two entities in each market so that the two companies could not join forces and create one, even larger, monopoly over both video and telephony services.

Given the uncertainties of telephone and cable competition, a restriction on the incumbents' ability to own LMDS licenses could be even more important than the so-called cable-telephone cross-ownership ban in the Telecommunications Act. Telephone companies

---

promote the policies and purposes of this Act favoring diversity of media voices, vigorous economic competition, technological advancement, and promotion of the public interest, convenience, and necessity." CPI believes that limiting the eligibility of incumbents for LMDS licenses satisfies each one of these goals.

[3] First Report and Order and Fourth Notice of Proposed Rulemaking, para. 14. (NPRM)

[4] See new Section 652 of the Communications Act of 1934.

have been free for over 2 years to enter the cable business. While several trials are now underway, it is as yet unclear whether the economics of telephone company entry into cable will allow the telephone companies to compete effectively for video services using their existing networks. The same is true for cable operators' entry into the telephone market. The cable industry has been seeking for several years to develop modems that will allow them to carry data traffic over their coaxial cable lines. To date, cable modems have not been widely deployed, and technical and economic problems remain. Even these cable modems, however, would not allow cable companies to provide voice telephony over their wires.

Because LMDS is a wireless operation that does not involve laying new wires or upgrading existing plant, LMDS may provide competition to the incumbent telephone companies and cable operators more quickly than one of the existing participants. While there are certainly technical issues surrounding the LMDS technology, the Commission cannot be certain at this point which technology will succeed.

Furthermore, even if the telephone companies and cable companies are able to enter each other's markets, the Commission should not assume that two competitors in a market will be sufficient for a market to become competitive. The Commission itself acknowledged a few years ago that its policy decision to issue two cellular licenses in each market did not result in a "fully competitive" market. This is one reason why the FCC decided to issue several new wireless licenses to provide Personal Communications Services. The Department of Justice also recognized that the duopoly cellular market was not fully competitive when it considered AT&T's acquisition of McCaw Cellular Communications a few years ago. While the entry of a third competitor in a market does not guarantee that a market will become competitive, it certainly is a step in the right direction.

Given the nascent stages of competition and technology in both the video and telephony markets, the FCC should be particularly careful that it does not take action in this proceeding to stifle the possibilities for competition at this stage. The Commission should consider strongly the benefits that a third entrant into the market can bring. If the Commission were to permit the incumbent carriers to invest in LMDS at this point, and if LMDS turns out to provide a significant alternative to traditional telephone and cable systems, we may forever lose the chance to see true competition develop in both of the video and telephony markets.[5]

III. The incumbent telephone companies and cable companies will have less of an incentive to exploit LMDS technology to its fullest extent in order to protect their existing services.

If the ILEC or the ICO is permitted to own an LMDS license in the same market where it currently provides telecommunications or video services, it will not have the same incentives to develop the LMDS technology to its fullest extent. This is because the cable company and the telephone company must balance the additional revenues from acquiring LMDS subscribers with the potential loss of revenue from its traditional services. This potential loss of revenues from its existing services may discourage the ILEC or the ICO from developing the full-service capability of the LMDS technology, even if consumers want the full services. No other applicants for this technology, other than the incumbents in that particular market, would have these incentives.

For instance, if the ILEC obtains the LMDS license, it will have the choice of deciding

[5] To be frank, it will be much easier to remove a cross-ownership restriction later if it is found to be unnecessary than to impose such a restriction after either the cable companies or telephone companies have made substantial investments in the technology.

whether to provide telephony-like services, video-like services, or both. In making this decision, the ILEC must evaluate the possibility that additional revenue gained from acquiring LMDS subscribers for telephony-like services will be accompanied by a decline in traditional telephone revenues, especially if the subscriber replaces his or her telephone service with LMDS. Further, a decline in revenues from its traditional telephone services (or even a reduction in the rate of growth of such services), is unlikely to reduce the ILEC's costs of providing such services. The telephone company's costs of providing telephone service are largely fixed, and costs per person rise the fewer users are on the network. In other words, the loss of a customer to LMDS is not likely to allow the ILEC to reduce its costs a great deal. There is thus some reason to believe that the telephone companies would prefer not to develop the telephony aspects of the LMDS technology in order to protect its existing investment in traditional telephone services.

Whether the loss of revenues from traditional telephone services is likely to be greater or lesser than the additional LMDS revenues is uncertain. The point is that the incentives of the telephone company to exploit the telephony services using the LMDS license will be less than the incentives of any other entity that could own that license.

Virtually the identical analysis applies to the ICO in that market. The ICO also has huge fixed investment in the ground that it will have certain incentives to protect. For every customer that signs up to receive video service from the LMDS licensee, the cable company risks losing revenues from its traditional cable service.[6] Yet its costs of providing cable service are not likely

---

[6] The record demonstrates that LMDS could be used to provide as many as 200 digital channels of video programming directly to consumers' homes. Many of the consumers that subscribe to LMDS video offerings are likely to substitute LMDS for their cable service. For instance , the FCC received evidence in its DBS decision that 80% of consumers who subscribe

to decline much at all. For this reason, the cable company will have less of an incentive to develop the video services that LMDS may be capable of providing.

Consumers will benefit most from a policy that gives the LMDS license in each market to an entity that has the maximum incentives to develop both the video and telephony services that LMDS is capable of providing. LMDS is a dynamic and uncertain technology whose deployment can be influenced strongly by the incentives of the owners of the license. Both the ILEC and the ICO have diminished incentives to develop one or the other of the types of services. No other entrant would face those same incentives. Consumers will best be served by companies that are trying as best they can to provide the full range of LMDS services.

IV. An eligibility restriction for LMDS licenses is comparable to several cross-ownership restrictions that Congress and the FCC have adopted in the past.

Congress did not consider restrictions on the eligibility of incumbents for LMDS when it enacted the Telecommunications Act of 1996. Nevertheless, eligibility restrictions on LMDS licenses are comparable to several different cross-ownership restrictions adopted by the FCC and by Congress in the past.

The 1984 Cable Act restricted cable operators from owning licenses to provide Multichannel Multipoint Distribution Service (MMDS) in the same market. The Telecommunications Act of 1996 retained, but modified, this cross-ownership restriction in

---

to DBS service canceled or reduced their cable service. See, In the matter of Revision of Rules and Policies for the Direct Broadcast Satellite Service, Report and Order, December 15, 1996 (IB Docket No. 95-168; PP Docket No. 93-253) para. 48. (DBS Auction Decision)

Section 613(a) of the Communications Act.[7] This provision was enacted out of a desire to encourage MMDS to become an alternative to, not a supplement of, traditional cable service.

The FCC, in its rules, and the Cable Act of 1984, banned telephone companies from the provision of cable service in the same market. Although this restriction was invalidated by the courts and subsequently repealed by the Congress in the Telecommunications Act, it is another example of a cross-ownership restriction that lasted for several years and that provides a precedent for the Commission's adoption of a similar restriction for LMDS.[8]

The FCC has also adopted eligibility restrictions concerning similar services. For instance, the Commission made existing cellular companies ineligible for certain PCS licenses, and, in the early 1980's, the Commission ruled that telephone companies would not be eligible for certain cellular licenses in their services areas.

Further, LMDS eligibility is related to the eligibility of cable operators in the auction for the DBS slot at 110 degrees. In the DBS Auction Decision,[9] the Commission declined to adopt restrictions that would have prevented cable operators from bidding for the DBS license at 110 degrees. The Commission stated

> We share the concern that cable-affiliated MVPDs [Multi-Video Program Distributors] with market power could use DBS resources, including those soon to be available at

---

[7] The Telecommunications Act amended the cable-MMDS cross-ownership restriction by adding a new paragraph (3). The effect of this new paragraph is to sunset the restriction once a cable operator faces "effective competition." This policy is similar, but not identical, to the policy recommendation of CPI, discussed below.

[8] In contrast to the policy that CPI suggests with regard to LMDS eligibility, the cable-telephone cross-ownership restriction did not have an explicit "sunset".

[9] Para. 73.

> auction, for coordinated conduct that would not maximize competition in the MVPD market and would therefore fail to give the public the benefits that flow from vigorous competition.

The Commission declined to adopt a restriction on cable participation in the DBS auction, however, largely because there would be two other DBS providers. "The presence of these other providers severely constrains the strategic activities of an MVPD-DBS combination, since even if it chooses not to make full use of its DBS channels, consumers will have at least two other competitive sources of DBS service from which to choose." In contrast, the Commission will only be issuing one LMDS license in each market. If the cable operator or ILEC acquires the sole LMDS license, it will not face competitive forces from other LMDS providers in that market. The lack of such intra-industry competition makes it more likely that the incumbent owner of the LMDS license will fail to develop the full potential of the technology in order to protect its existing investment.

V. <u>The efficiencies of providing LMDS and cable or telephony services are minimal and should not be given much weight in this decision.</u>

Other commenters in this proceeding are better equipped to discuss the technical operations of LMDS networks compared to cable and telephone networks. CPI simply suggests the following considerations should affect the FCC's analysis of the question of efficiencies. First, CPI believes the efficiencies that could be gained from offering LMDS along with cable and telephone service are minimal. Obviously, LMDS is a wireless network, while ILEC and ICO networks currently use wires, reducing the potential for any cross-efficiencies. Second, any potential efficiencies of using telephone company plant and operating an LMDS network is already being addressed through the unbundling and resale provisions that the Commission and the States are adopting to implement the Telecommunications Act. These provisions will allow LMDS licensees to purchase and share the facilities of ILECs at prices based upon the incremental cost of providing such elements. Similarly, LMDS operators can lease space on cellular or PCS towers, or the buildings where such towers are located, to reduce the costs of antenna siting.[10]

Regardless of these arguments, CPI encourages the Commission not to focus too much attention on the potential efficiency losses involved in restricting the eligibility of ILECs and ICOs from LMDS licenses. If efficiency were the overriding goal, Congress would not have decided so unequivocally to encourage competition in all market sectors. It may well be more efficient to have one entity providing all long distance service, local telephone service, cable service, wireless services, satellite services, etc. For many years, the efficiency argument was used to justify the FCC's decisions to protect the monopoly of AT&T over telephone service. While those policies may have been the correct ones in the distant past, the Commission and Congress have long since discarded the efficiency arguments as reasons for continuing the role of the monopoly in communications. It is simply impossible for the Commission to determine at this nascent stage in the development of LMDS technology which company may or may not be able to provide the service most efficiently. Some might even argue that, should the FCC try engage in such a prediction of the future, the FCC would be engaging in "industrial policy", or that the FCC would be attempting to pick winners and losers.

---

[10] Further, to the extent that LMDS licensees provide a common carrier wireless exchange access service that falls within the definition of personal wireless services, the passage of Section 704 of the Telecommunications Act concerning facilities siting could also help to reduce the costs of building antennas for LMDS.

Simply put, rather than focusing on predictions of technological deployment, the FCC should focus more on the *incentives* of the carriers. Clearly, those companies that do not have a stake in protecting their existing investments have stronger incentives to develop the full potential of LMDS technology than those that do have existing investments to protect.

VI. The risks that incumbents will not develop LMDS to its fullest potential cannot be addressed in any manner other than restricting eligibility.

A. Build-out requirements are not sufficient.

Some parties suggest that any concerns about the incentives of incumbents to warehouse the LMDS license can be addressed by build-out requirements. As discussed above, however, a requirement to build out a certain amount of *facilities* does not address the incentives to provide certain *services* over their facilities. A cable operator could well satisfy a requirement to construct a certain number of antennas or provide a certain amount of coverage and yet delay its provision of video services over their facilities. The same is true concerning telephone companies' incentives not to provide telephony services. CPI suggests that the Commission should not rely upon build-out requirements to overcome the incentives of incumbents to protect their existing investments.

B. The Commission should not attempt to limit the type of services provided by an LMDS licensee.

The Commission suggests that one option would be to limit ILEC participation in LMDS to a certain percentage of non-video programming, and cable participation to a certain percentage of video services. CPI believes this approach would not be practical. The Commission would have a difficult time determining what services are video and which are not, for instance. Even if it could make this determination, it is difficult to know how to enforce a particular percentage, especially because the nature of digital technology makes it difficult to compare numbers of bits, and because the technology allows dynamic uses of the spectrum which may change constantly. Further, it would involve the FCC in an overly regulatory solution that itself could retard the technology and delay the provision of service to consumers.

VII. The Commission should bar ILECs and ICOs from acquiring LMDS licenses in their services areas in the auction and afterwards.

The Commission should prohibit ILECs and ICOs from acquiring LMDS licenses both in the auction and afterwards in the marketplace. If the Commission agrees that the ILECs and ICOs should not be eligible in the auction, it would undercut the Commission's policies to allow the ILECs and ICOs to purchase the license after the auction in the secondary marketplace. If the Commission were to allow the incumbents to purchase the license afterwards, some bidders might enter the auction bidding solely for the purpose of reselling the license in the secondary market. In addition to the dangers to consumers discussed above, the additional transaction costs of putting a license out for bid in the secondary market by someone who is not interested in providing service, and the process involved in negotiating the purchase terms, could further delay service to the public.

The Commission should also place strict limits on any financial relationship between an incumbent and an LMDS licensee. Congress chose to limit ILECs and ICOs to a 10% financial interest, and to prohibit any management interest, in each other when enacting the prohibition on cable-telephone buyouts. A similar threshold would be appropriate for LMDS licenses. The Commission should make clear that financial interests could include an equity interest, debt interest, or contractual interest, or other financial interest.

VIII. The Commission should remove the prohibition only after the ILEC or ICO demonstrates that it faces true market competition.

The Commission suggests that any restriction on ownership should continue only until there is increased competition in the video and telephony markets. CPI agrees with the thrust of this approach, with a few clarifications. First, CPI believes that the burden should be placed on the ILEC and the ICO to demonstrate that it faces true competition in the market before it is allowed to purchase the LMDS license.[11] The ILECs and ICOs have been claiming that they face competition for years, despite overwhelming evidence to the contrary. The Commission should not allow these entities to self-certify that they face competition, or the eligibility restriction would end up having no practical effect.

Further, the competition must exist from services other than the services being provided by the LMDS licensee. In other words, the ILEC and the ICO must demonstrate that they will face such competition *after* they acquire the LMDS license.

CPI disagrees with the suggestions that the definition of "effective competition" in Section 623(l) of the Communications Act and compliance with the "checklist" by the ILECs should be the standards for determining when the prohibition should sunset. Both of these standards were developed for other purposes, and neither of which is sufficient to determine whether an ILEC or ICO faces true marketplace competition. The standard of effective

[11] This demonstration could be made either in a general rulemaking proceeding, or in a case-by-case determination at the time application is made to acquire the LMDS license, whichever is less burdensome to the incumbents and the Commission.

competition for cable operators was developed to determine when rate regulation of the cable system should or should not apply. That definition can be triggered in many cases whether a market is truly competitive or not. (For instance, the Act says the "effective competition" test is met if less than 30% of subscribers actually subscribe to cable service, or if a municipality offers its own cable service to over 50% of the population in an area, whether the market is competitive or not.)

Similarly, the "checklist" was developed as one of several preconditions that an RBOC must face before it is allowed to provide interLATA service. While the unbundling rules are important to competition, there are many other factors that affect the competitiveness of a market, including technological, financial, economic factors. Further, as the Commission noted, the "checklist" in Section 271 of the Communications Act does not apply to ILECs other than the RBOCs.

The FCC further suggests the possibility of sunsetting the prohibition after three years. We do not support an arbitrary time period for eliminating the prohibition. An arbitrary time period gives the incumbents incentives to delay competition until the time period expires. CPI suggests instead that the Commission should agree at this time that it will conduct a review of the ownership restriction no later than three years after it adopts the rules in this proceeding. Nothing should preclude the Commission from reviewing the restriction earlier than three years, either on a case-by-base basis or in a general proceeding. Any decision to remove the prohibition must be tied to the actual competition in the market.

IX. The Commission should determine who is an incumbent based on a percentage of homes "passed", not homes served.

The FCC asks how much of an LMDS license area an ILEC or ICO must serve in order to be ruled ineligible for an LMDS license. CPI is not prepared at this time to advise the Commission what percentage of homes a cable operator or ILEC should pass in an LMDS service area in order to be considered ineligible in that market. CPI notes, however, that whatever percentage is adopted should be tied to the percentage of homes "passed", not the percentage of homes served or the percentage of homes authorized to be served. ILECs and ICOs have incentives to protect their investments that are in the ground, whether the subscriber takes the service offered over such facilities or not. This is particularly important for cable companies that may pass 90 to 95% of homes but who may actually provide service to 60 to 65% of homes.[12] Also, to the extent an ILEC or ICO is authorized to serve certain households but has not yet built facilities to serve that customer, the ILEC or ICO may have the same incentives to deploy LMDS to those homes as any other applicant. Therefore, the percentage should be based on the percentage of homes "passed", in other words, where facilities have already been invested.

[12] CPI will make such a suggestion in its reply comments.

X. Conclusion

CPI appreciates the FCC's invitation for comments in this proceeding concerning eligibility. LMDS could provide a significant opportunity for competition to develop in telephony and video services. Preventing incumbent telephone companies and cable operators from acquiring LMDS licenses in their markets could be absolutely critical to giving consumers an opportunity to benefit from such competition.

Respectfully Submitted,

John Windhausen

John Windhausen, General Counsel
Ronald J. Binz, President
Debra Berlyn, Executive Director

Competition Policy Institute
1156 15th St. N.W. Suite 310
Washington, D.C. 20005
202 835-0202 202 835-1132 (fax)